The Weekly Snapshot

3 July 2023

ANZ Investments brings you a brief snapshot of the week in markets

Most major global equity markets ended the week higher, rounding off not only a strong second quarter, but also a solid first half to the year.

In the US, the S&P 500 Index finished up 2.4%, while the NASDAQ Composite Index gained 2.2%. In fact, the tech-heavy NASDAQ Composite Index has had its best first half to a year since 1983.

It was a similar story in Europe, with Germany's DAX Index up 2.1% and the UK's FTSE 100 Index up 1.0%. Japanese shares continued their strong run, with the Nikkei 225 Index up 1.2%.

New Zealand shares took their lead from their international counterparts. The NZX 50 Index rose 1.5%, while across the Tasman, the ASX 200 Index finished up by the same amount.

Bond markets trended lower in price terms. The yield on the US 10-year government bonds rose 10 basis points to 3.84% following a larger-than expected upward revision to US Q1 GDP (annual growth of 2.0%, versus 1.2% previously). New Zealand bonds also came under some pressure as the market absorbed additional bond supply. The yield on the 10-year government bond rose 9 basis points to 4.64%.

What's happening in markets?

Share markets were given a boost late in the week when the US Federal Reserve's (the Fed's) preferred measure of inflation – the Personal Consumption Expenditures price index – showed a cooling off in May. The PCE price index rose 3.8% over the year to end May, down from 4.3% in April. On a monthly basis, prices were up a mere 0.1%.

Meanwhile, the core PCE price index, which is more closely watched by the Fed policy makers (since it strips out volatile food and energy prices), rose 4.6%, down from 4.7% previously, and is at its lowest level since October 2021. While the data shows inflation moving gradually in the right direction, it's still well above the Fed's 2% long-term target level.

The inflation data came on the back of some interesting (if not contradictory) talk from members of the Fed. Firstly, Fed Chairman, Jerome Powell, said the central bank was open to consecutive rate hikes at its upcoming meetings, because there was a chance the tight labour market could contribute to an uptick in inflation. Meanwhile, Atlanta Fed President, Raphael Bostic (a non-voting member), said he doesn't see as much urgency to move as others, adding that the economy is only now starting to see the impacts of monetary tightening.

Despite the opposing views, interest rate markets have moved to price in an 83% chance of a further quarter precent rates hike at its 25-26 July meeting, up slightly from a week ago.

Across the Tasman, there was some mixed economic data. Australian inflation fell to a 13-month low in May, driven mainly by a fall in fuel prices. The Consumer Price Index (CPI) showed a 5.6% increase in the year to May, marking the smallest increase since April last year. Core inflation also rose at a lower annual pace of 6.1%. The softer numbers are a sign the Reserve Bank of Australia (RBA) may not need to raise interest rates further at their meeting later this week.

However, offering conflicting messages was Australian retail sales data, which climbed by more than expected in May, suggesting that household spending remains resilient in the face of rising interest rates. Sales were up 0.7%, compared to the 0.1% expected. Retail sales are an important factor in rate decisions, since consumption accounts for around 60% of GDP (Gross Domestic Product), and so policy makers at the RBA will need to decide whether or not this means higher interest rates can be tolerated.

Meanwhile, in New Zealand, the key economic data out was the ANZ Business Outlook Survey. It showed that business confidence jumped 13 points in June, to hit its highest level since November 2021. June's survey showed a net 18% of businesses expect economic conditions to weaken over the year ahead, although this is an improvement from a net 31% in May. Firms' expectations for their own trading also turned positive for the first time in 14 months.

What's on the calendar?

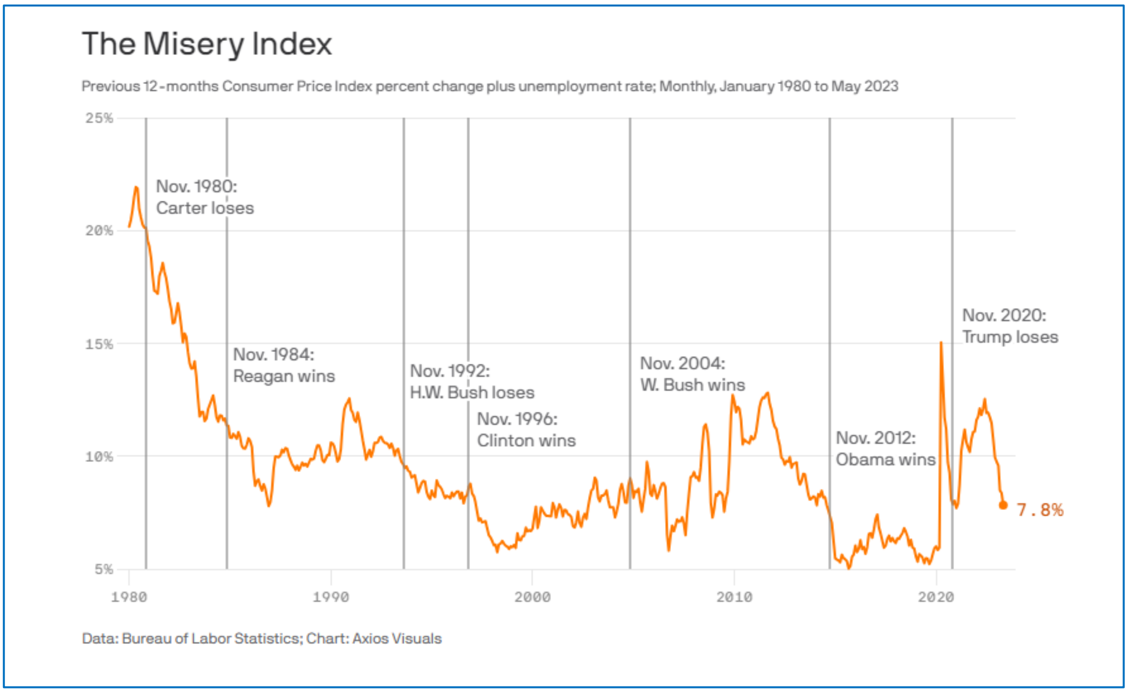
On Thursday, minutes from last month's Fed meeting will give insights into why the central bank paused and hopefully provide more colour as to why the Fed's median dot plot suggests two more rate hikes are on the cards for later this year.

Elsewhere, the focus will be on the US and developed market PMIs (Purchasing Manager Indexes) for June. Preliminary figures showed an acceleration in the pace of deterioration in manufacturing activity, while services activity was also slightly weaker across the board. The final numbers are expected to show a similar theme; with the US holding up better than in Europe and the UK.

Arguably the most important data print will be employment data late in the week. In May, this delivered a strong positive surprise, with a 253,000 change in nonfarm Payrolls versus 185,000 expected. The market currently expects the change in nonfarm payrolls to be 200,000 which is still elevated by historical standards. However, a meaningful deterioration in the labour market is likely required for the Fed to consider easing monetary policy.

Chart of the week

The 'Misery Index', which is created by adding together the unemployment rate and inflation, has fallen significantly over the last year. Created by economist Arthur Okun, it's a somewhat crude but effective way of measuring how the average citizen is doing financially. Read more below.



Here's what we're reading

The 'Misery Index is falling fast. The current mix of U.S. unemployment and inflation is entirely consistent with rates that have historically tended to get presidents re-elected: https://www.axios.com/2023/06/26/misery-index-falling-fast

AI's winners, losers and wannabes – An NVIDIA valuation, with the AI Boost: https://aswathdamodaran.blogspot.com/2023/06/ais-winners-losers-and-wannabes-nvidia.html

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